

Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 IO-10 XMB-02 AGR-05 CEA-01 CIAE-00

COME-00 DODE-00 EB-07 FRB-03 H-01 INR-07 INT-05 L-02

LAB-04 NSAE-00 NSC-05 PA-01 AID-05 CIEP-01 SS-15

STR-01 TAR-01 TRSE-00 USIA-06 PRS-01 SP-02 FEAE-00

OMB-01 OPIC-03 /100 W

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R 211413Z FEB 75

FM AMEMBASSY MONTEVIDEO

TO SECSTATE WASHDC 8286

INFO AMEMBASSY BRASILIA

AMEMBASSY BUENOS AIRES

C O N F I D E N T I A L SECTION 1 OF 2 MONTEVIDEO 0570

E.O. 11652: GDS

TAGS: PINT, ECON, ELAB, AFSP, ETRD, UY

SUBJ: GOU ECONOMIC POLICY: SOME MEASURES

AGREED TO BUT DEBATE TO CONTINUE

REF: A) MVD 364, B) MVD 3656 (1974),

C) MVD 3337 (1974)

1. SUMMARY: AS HAS BEEN PREVIOUSLY REPORTED (REF A), THE GOU HAS BEEN ENGAGED IN AN INTERNAL DEBATE OVER FUTURE ECONOMIC POLICY. THE DEBATE CENTERS AROUND TH AUTHORITY OF MINECON VEHG VILLEGAS TO DIRECT ECONOMIC POLICY, A WAGE/PRICE FREEZE, EXTENT OF DEVALUATION, IMPORT LIBERALIZATION AND CONTROL OF CREDIT EMISSION BY THE BANK OF THE REPUBLIC (BOR). VEGH, REPORTEDLY, TWICE SUBMITTED HIS RESIGNATION DURING THE COURSE OF THE DEBATE BUT AT THE STRONG URGING OF KEY MILITARY AND CIVILIAN LEADERS, HE WAS PERSUADED TO STAY ON. ON FEB 8, THE GOU ANNOUNCED A SERIES OF ECONOMIC MEASURES UPON WHICH AGREEMENT HAD BEEN REACHED. THESE MEASURES REFLECTED SOME PROGRESS ON BUDGET AND MONETARY MATTERS AND ON CAPITAL GOODS IMPORT LIBERALI-
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ZATON. THE DEBATE OVER THE UNRESOLVED ISSUES (INCOMES

POLICY, BOR CREDIT EMISSION, COMPLETE IMPORT LIBERALIZATION)
IS EXPECTED TO CONTINUE. VEGH'S WITHDRAWAL OF HIS RESIGNATION
MAY BE TAKEN AS A SIGN THAT HE IS SATISFIED WITH GOU SUPPORT
FOR HIS PROPOSALS AND REFLECTS HIS CONFIDENCE THAT HE WILL
EVENTUALLY BE ABLE TO NEGOTIATE AN IMF STANDBY. END SUMMARY.

2. THE GOU ANNOUNCED THE FOLLOWING ECONOMIC MEASURES:

A) WAGE INCREASES-A MINIMUM INCREASE OF 15 PERCENT FOR
PRIVATE SECTOR EMPLOYEES RETROACTIVE TO FEB 1. EXCEPT FOR
SPECIAL CASES TO BE DETERMINED BY THE WAGE AND PRICE
COMMISSION (COPRIN) ONLY 5 PERCENT OF THIS INCREASE MAY BE PASSED
ON TO CONSUMERS IN INCREASED PRICES; THE REMAINING 10 PERCENT AND
ANY ADDITIONAL INCREASES WHICH MAY BE GRANTED OVER THE
MINIMUM MUST BE ABSORBED BY EMPLOYERS. THE MINIMUM
WAGE FOR URBAN WORKERS WAS INCREASED TO UP\$5,520 (ABOUT
US\$2.40) PER DAY OR UP\$138,000 (ABOUT US\$60.00) PER MONTH.
GOVERNMENT WORKERS WILL RECEIVE A 15 PERCENT WAGE INCREASE BEGINN-
ING MARCH 1. THE MONTH'S DELAY PROBABLY HAS THE EFFECT OF
REDUCING THE INCREASE BY OVER 50 PERCENT IN REAL TERMS FOR GOVERN-
MENT WORKERS DUE TO THE RECENT 8 PERCENT TO 10 PERCENT MONTHLY
RATE OF INFLATON. PENSIONS WILL BE INCREASED BY 25 PERCENT BEGIN-
NING MARCH 1, PENDING APPROVAL OF A BILL BY THE COUNCIL OF STATE AUTH
ORIZING
ADVANCE PAYMENT OF THE ANNUAL PENSION READJUSTMENT REGULARLY
SCHEDULED FOR JULY.

B) PRICE INCREASES-PRICE INCREASES WERE DECREED
FOR A WIDE RANGE OF PRODUCTS AND SERVICES ALONG THE FOLLOWING
GENERAL LINES:

1. INCREASES FROM 40 TO 50 PERCENT-REGULAR GASOLINE,
TELEPHONE, ELECTICITY, WHEAT FLOUR AND FUEL OIL.
2. INCREASE FROM 31 TO 40 PERCENT-BREAD, PASTAS,
HIGH OCTANE GASOLINE AND OTHER PETROLEUM PRODUCTS.
3. INCREASES FROM 21 TO 30 PERCENT-BEEF, WATER
SERVICES AND BUS FARES.
4. INCREASES FROM 11 TO 20 PERCENT-RICE, MILK,
PRICES IN RESTAURANTS AND BARS, CIGARETTES, TAXI FARES AND
MEDICAL SOCIETY CONTRIBUTIONS.
5. INCREASES 10 PERCENT AND UNDER-TEXTILES, LEATHER
GOODS, WOOD PRODUCTS, CONSTRUCTION MATERIAL, GLASS, CHEMICALS,
RUBBER PRODUCTS AND VARIOUS OTHER MANUFACTURED PRODUCTS.

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6. GOODS AND SERVICES EXEMPT FROM PRICE
INCREASES WERE: COOKING OIL, PORK PRODUCTS, NATURAL GAS,
FERTILIZERS, CARS, PRIMARY AND SECONDARY SCHOOL TUITION,
AND ALL GOODS NOT SPECIFICALLY NAMED IN THE DECREE.

C) EXCHANGE RATES-THE COMMERCIAL RATE OF EXCHANGE
WAS DEVALUED BY 6 PERCENT ON FEB 7, TO 1901 PESOS PER DOLLAR FOR
EXPORTS AND 1920 FOR IMPORTS. THIS WAS THE FIFTH CORRECTION

IN A PERIOD OF ABOUT TWO MONTHS AND BRINGS THE COMMERCIAL RATE TO A LEVEL ABOUT 20 PERCENT BELOW THE FLOATING FINANCIAL RATE. SINCE DEC 1, THE COMMERCIAL RATE HAS BEEN DEVALUED BY 28 PERCENT. IN A COMPLEMENTARY MEASURE, CONSULAR FEES ON IMPORTS WERE REDUCED FROM 12 PERCENT TO 6 PERCENT OF FOB VALUE. THIS ALLOWED THE GOU TO DECREE THAT THE 6 PERCENT INCREASE IN IMPORT COSTS DUE TO THE DEVALUATION WOULD NOT BE PASSED ON TO CONSUMERS IN INCREASED PRICES.

D) CAPITAL GOODS IMPORT LIBERALIZATION-REGULATIONS COVERING IMPORTS OF CAPITAL GOODS WERE CHANGED TO ELIMINATE THE POSTING OF ADDITIONAL PRIOR DEPOSITS (CONSIGNACIONES) WHICH, IN EFFECT, ENDS THE PRESENT QUOTA SYSTEM FOR "CAPITAL GOODS".

FINANCING REQUIREMENTS WERE ALSO EASED SO THAT IMPORTS DURING THE CALENDAR YEAR BY ANY ONE FIRM FOR ITS OWN USE TOTALING \$20,000 OR LESS REQUIRE NO EXTERNAL FINANCING; IMPORTS FROM \$20,000 TO \$100,000 NOW REQUIRE 3 YEARS FINANCING, AND IMPORTS OVER \$100,000 REQUIRE 5 YEAR FINANCING. PREVIOUS REGULATIONS REQUIRED 5-YEAR FINANCING FOR IMPORTS VALUED OVER \$20,000. A COMMISSION WAS CREATED WHOSE RESPONSIBILITIES ARE TO COMPILE A LIST OF PRODUCTS WHICH SHALL BE DESIGNATED AS "CAPITAL GOODS", TO SET UP RULES GOVERNING IMPORTS OF "CAPITAL GOODS" BY RETAILERS OR DISTRIBUTORS AND TO AUTHORIZE MORE LENIENT FINANCING TERMS THAN THOSE STIPULATED ABOVE ON A CASE-BY-CASE BASIS.

E) CATTLE PRICES-THE NOV 20, 1974 DECREE RAISING CATTLE PRICES TO THE PRODUCER BY 20 PERCENT WAS RESCINDED. DEBATE OVER THE BOR'S UNILATERAL REFUSAL TO PAY THE INCREASED PRICES--THUS FLOUTING MINISTERIAL AUTHORITY--WAS THE OCCASION FOR THE FIRST OF VEGH'S RESIGNATIONS, DESCRIBED BELOW.

F) PROBLEM OF EXCESS CATTLE-IN RESPONSE TO INSISTENT PRODUCER DEMANDS TO DEAL WITH THE PROBLEM OF EXCESS CATTLE ON THE RANGE (ESTIMATED AT 2 MILLION HEAD) FOR WHICH THERE WILL

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NOT BE ADEQUATE PASTURAGE THIS COMING WINTER (I.E. JULY), THE GOU SET UP A COMMISSION TO STUDY THE PROBLEM AND REPORT WITHIN 15 DAYS ON RECOMMENDED MEASURES TO BE TAKEN. ONE POSSIBILITY BEING STUDIED, ALTHOUGH RELUCTANTLY, IS TO EXPORT LIVE CATTLE, POSSIBLE TO BRAZIL.

3. A BRIEF CHRONOLOGY OF THE DEBATE INsofar AS WE HAVE BEEN

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STR-01 TAR-01 TRSE-00 USIA-06 PRS-01 SP-02 FEAE-00

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FM AMEMBASSY MONTEVIDEO

TO SECSTATE WASHDC 8287

INFO AMEMBASSY BRAZIL

AMEMBASSY BUENOS AIRES

C O N F I D E N T I A L SECTION 2 OF 2 MONTEVIDEO 0570

E.O. 11652: GDS

TAGS: PINT, ECON, ELAB, AFSP, ETRD, UY

SUBJ: GOU ECONOMIC POLICY: SOME MEASURES AGREED TO BUT

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ABLE TO PIECE IT TOGETHER FOLLOWS: JAN 23-VEGH PRESENTED HIS RESIGNATION PROMPTED BY HIS UNHAPPINESS OVER THE REFUSAL OF BOR PRESIDENT GEN RAIMUNDEZ TO COMPLY WITH A NOV 1974 DECREE RAISING CATTLE PRICES 20 PERCENT TO PRODUCERS, WHICH INCREASE HAD TO BE ABSORBED BY THE BOR. RAIMUNDEZ REFUSED TO HONOR THE DECREE NOTING THAT CONSUMER PRICES WERE NOT ALSO RAISED AND ACCORDINGLY THAT THE BOR WOULD HAVE TO TAKE A LOSS. VEGH REPORTEDLY WITHDREW HIS RESIGNATION A FEW DAYS LATER AFTER THE PRESIDENT AND THE JUNTA DE COMANDANTES REAFFIRMED HIS AUTHORITY TO DIRECT ECONOMIC MEASURES WHICH WOULD BE IMPLEMENTED BY THE SUBORDINATE BOR. HOWEVER, THE MEASURE WAS LATER WITHDRAWN RETROACTIVELY IN WHICH VEGH CONCURRED, ATTRIBUTING HIS CHANGE TO THE RECENT DECLINE IN WORLD BEEF PRICES. FEB 3-WITH THE MEAT PRICE ISSUE DISPOSED OF, VEGH, DURING THIS WEEK, ARGUED HIS PROPOSED PROGRAM BEFORE
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THE JUNTA DE GENERALES (ACTIVE DUTY GENERAL AND FLAG OFFICERS FROM ALL SERVICES). GEN RAIMUNDEZ LED THE ATTACK ON VEGH'S PROGRAM.

HE OPPOSED VEGH'S PLAN FOR A LARGE DEVALUATION AND MORE SPECIFICALLY, THE PLAN TO ABOLISH THE IMPORT CONTROL SYSTEM, WHICH WOULD HAVE CUT OFF THE BOR FROM USING PRIOR DEPOSITS FROM IMPORTERS AS AVAILABLE LOAN FUNDS. FEB 4-VEGH AGAIN PRESENTED HIS RESIGNATION TO BORDABERRY EXPRESSING FRUTRATION AT NOT BEING ABLE TO CONDUCT ECONOMIC POLICY. HE WAS PARTICULARLY CONCERNED THAT HE HAD TO NEGOTIATE HIS PROPOSALS IN AN ATMOSPHERE WHERE HIS CRITICS FAILED TO PROVIDECONSTRUCTIVE ALTERNATIVESIN DEALING WITH THE COUNTRY'S BASIC PROBLEMS AND WHEREHE HAD TO NEGOTIATE EVERY DETAIL OF POLICY WITH A NUMBER OFMILITARY OFFICERS, EACH OF WHOM HAD DIFFERENT IDEAS ON HOW THE ECONOMY SHOULD BE MANAGED. PRES BORDABERRY REPORTEDLY SUPPORTED VEGH AND HIS PROGRAM BUT ALSO REPORTEDLY URGED THAT CERTAIN FEATURES OF THE PROGRAM NOT BE IMPLEMENTED UNTIL SUCH TIME AS THE INTERNATIONAL ECONOMIC SITUATION WAS FURTHER CLARIFIED. FEB 5-AT AT SPECIAL MEETING OF CABINE MEMBERS, ORGANIZED BY FOREIGN MINISTER BLANCO, ALL PRESENT EXPRESSED THEIR CONFIDENCE IN VEGH AND ASKED HIM TO WITHDRAW HIS RESIGNATION.FEB 6-7-VEGH WITHDREW HIS RESIGNATION AFTER FURTHER EXPRESSIONS OF SUPPORT WERE RECEIVED FROM THE PRESIDENT AND THE JUNTA DE COMANDANTES. AT THE SAME TIME A COMPROMISE WAS REACHED UNDER WHICH THE ECONOMIC MEASURES ON WHICHAGREEMENT WAS REACHED WOULD BE ANNOUNCED, THAT VEGH WOULD ADDRESS THE NATION ON FEB 21 TO EXPLAIN HIS PROGRAM, THAT DISCUSSIONSWITH THE JUNTA DE COMANDANTES WOULD CONTINUE ON FURTHER MEASURES TO BE TAKEN TO MEET IMF STANDBY CONDITIONSAND THAT RAIMUNDEZ WOULD JOIN VEGH'S ECONOMIC TEAM AND COOPERATE THEREIN.

4. COMMENT: CERTAIN KEY ISSUES NECESSARYFOR CONSIDER- TION OF AN IMF STANDBY WERE NOT COMPLETELY RESOLVED. IN A TYPICAL URUGUAYAN RESPONSE TO A CONFLICT SITUATION, SOME KEY DECISIONS WEREPOSTPONED AND A PRAGMATIC COMPROMISE WAS ARRIVED AT. IT IS QUITE UNDERSTANDABLE THAT A MAJOR CONTROVERSY AROSE OVERVEGH'S PROGRAM,WHICH IMPLIES A SUBSTANTIAL DOSE OF AUSTERITY INCLUDING SOME FURTHER DECLINE IN REAL INCOME AS WELL AS POLICY REFORMS WHICH COULD THREATEN A NUMBER OF VESTED INTERESTS IN THE PUBLIC AND PRIVATE SECTORS. IT WOULD APPEAR THATTHE ARMY HIGH COMMAND, FEARFUL OF THE CONFIDENTIAL

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EFFECTS THE CONFRONTATION BETWEEN VEGH AND RAIMUNDEZ WOULD HAVE ON DELICATELY BALANCED MILITARY UNITY, AND UNCERTAIN AS TO THE ECONOMIC-SOCIAL IMPLICATIONS OF VEGHS PROGRAM, AGREED TO DELAY A DEFINITIVE DECISION ONTHE PROGRAM, HOPING THAT FURTHER DIRECT CNSULTATIONS BETWEEN THE CONTESTING PARTIES COULD SOMEHOW RESOLVE THE ISSUES. VEGH HAS PROFITED BY THE COURSE OF THESE DEBATES, LEARNING THT HEMUST EDUCATE HIS AUDIENCE, THE MILITARY AND THE WIDER PUBLIC, ON THE DESIRABILITY OF HIS PROGRAM AND OBTAIN THEIR SUPPORT. RAIMUNDEZ

LEARNED THAT NEGATIVE CRITICISM OF VEGH'S PROGRAM HAS TO BE MATCHED BY CONSTRUCTIVE SOLUTIONS AND THAT HE COULD BE THE SCAPEGOAT IF VEGH'S DEPARTURE RESULTED IN A SACRIFICE OF PROMISED INTERNATIONAL ASSISTANCE. THE JUNTA DE COMANDANTES LEARNED THAT THEY ARE INSTITUTIONALLY INCAPABLE OF DECIDING COMPLEX ECONOMIC ISSUES BEYOND THEIR COMPREHENSION.

5. A DETERMINING FACTOR IN THE OUTCOME OF THIS PHASE OF THE DEBATE WAS THE REPORTED RELUCTANCE OF THE ARMY HIGH COMMAND TO CHOOSE BETWEEN VEGH AND RAIMUNDEZ AT THIS TIME. IF VEGH RESIGNED, THE GOU'S IMAGE IN THE INTERNATIONAL FINANCIAL COMMUNITY WOULD SUFFER AND THERE WOULD BE DIFFICULTY IN RECRUITING A REPLACEMENT. ON THE OTHER HAND, IF RAIMUNDEZ WERE OVERRULED OR RESIGNED FROM HIS KEY BOR POSITION, IT COULD PROVOKE A SPLIT AND PROBABLY AN UNWELCOME DEFINITION OF LOYALTIES IN THE ARMY HIGH COMMAND. IN ADDITION, RAIMUNDEZ FOR BETTER OR WORSE HEADS AN INSTITUTION (THE BOR) THAT REPRESENTS THE TRADITIONAL PATERNALISTIC CONTROL OF THE ECONOMY THAT VEGH WOULD LIKE TO SEE DISMANTELED. THUS, THIS PHASE OF THE DEBATE WAS RESOLVED PRAGMATICALLY BY ANNOUNCING THOSE MEASURES ON WHICH AGREEMENT HAD BEEN REACHED AND PUTTING OFF THE UNRESOLVED ISSUES FOR FURTHER NEGOTIATIONS. IN ADDITION, IN AN ATTEMPT TO HEAD OFF POLICY CONFLICTS BEFORE THEY REACHED THE CONFRONTATION STAGE, RAIMUNDEZ REPORTEDLY HAS OFFERED TO JOIN VEGH'S ECONOMIC TEAM IN FORMULATING POLICY. WHETHER OR NOT VEGH AND RAIMUNDEZ WILL BE ABLE TO COOPERATE REMAINS TO BE SEEN.

6. THE UNRESOLVED ISSUES REMAIN (A) CONTROL OF BOR CREDIT EMISSION, (B) INCOME POLICY AND STABILIZATION AND (C) FURTHER CHANGES IN IMPORT CONTROL SYSTEM. ONE VERSION HAS IT THAT THE GOU, WHILE DEFINITELY PLANNING A WAGE AND PRICE FREEZE, IS HOLDING OFF UNTIL A MORE OPPORTUNE MOMENT, WHEN PUBLIC

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EXPECTATION OF SUCH ACTION WILL HAVE SUBSIDED SOME INFORMATION MAY BE PROVIDED IN VEGH'S ADDRESS TO THE NATION SCHEDULED FOR FEB 21. WHETHER OR NOT THE GOU WILL EVENTUALLY TAKE THE MEASURES NECESSARY FOR IMF STANDBY REMAINS TO BE SEEN. VEGH AND HIS TEAM EXPRESS FULL CONFIDENCE THAT THEY WILL BE ABLE TO NEGOTIATE SUCCESSFULLY A STANDBY. VEGH'S WITHDRAWAL OF HIS RESIGNATION AND READINESS TO CONTINUE NEGOTIATIONS INDICATE THAT HE CONSIDERS HIS CHANCES OF OBTAINING A COHERENT ECONOMIC PROGRAM, ACCEPTABLE TO THE IMF AND IBRD, ARE FAVORABLE.

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